management's discussion and analysis

Financial Analysis

The Group recorded a 23.7% growth in turnover to HK$16.30 billion for the year with strong organic growth from all divisions. Net profit increased by 39.1% to HK$938 million with improved margins of 5.8% (2003: 5.1%).

Earnings per share were HK70.11 cents (2003: HK51.56 cents), an increase of 36.0%. Return on shareholders' funds increased to 27.3% as compared to 26.8% in 2003.

Gross Margin

Gross margin continued to improve, increasing to 30.3% from 29.6% despite higher raw material prices during the year. This reflected the Group's successful and well-balanced strategy to improve margins by continually introducing new products, expanding product categories, capitalizing on the well-recognized brand portfolio, leveraging business volume and economies-of-scale. These initiatives were aided by a highly effective program of ongoing cost improvement at all levels within the Group.

Selling, Distribution, Advertising and Warranty Expenses

Total expenses as a percentage of the Group's turnover improved to 11.8% from 11.9% in 2003. This represented an increase of only 21.7% to HK$1,917 million on the back of a 23.7% growth in turnover, reflecting the Group's ability to maintain its current cost structure while executing effective sales and marketing programs and improving overall efficiencies.

The Group's branded businesses accounted for 72.2% of total turnover as compared to 68.0% in 2003. The Group considered this increase to be consistent with its growth strategy. The percentage is expected to further increase with the addition of the Milwaukee, AEG and DreBo businesses to the Group's stable of brands.

Research and Development Expenses

Research and development expenses for the year amounted to HK$339 million, representing 2.1% of turnover, and an increase of 26.4% as compared to the HK$268 million or 2.0% of turnover in 2003. The Group will continue to invest in the design and development of high quality, innovative products and marketing concepts as it believes this is critical to maintaining long-term growth momentum.

Administrative Expenses

Administrative expenses increased mainly due to the full-year consolidation of Royal and additional goodwill amortized on the Royal acquisition, whereas in 2003, the year in which Royal was acquired, there were only 8 months of consolidation. In respect of the change in accounting policy for goodwill, the Group has not opted for early adoption of the new HKFRS 3 in respect of the 2004 results. Staff costs during the year also increased following the Group's decision to improve overall staff quality and management resources in preparation for the growth challenges ahead.

Taxation

The effective tax rate for the year was 10.0%. The Group will continue to capitalize on its global operations for more effective tax planning.

Liquidity and Financial Resources

Shareholders' Funds

Total shareholders' funds amounted to HK$3,439 million as at 31st December, 2004, representing an increase of 36.8% from HK$2,513 million as reported last year. Book value per share, after the increase in the number of shares issued due to the exercise of options during the year, rose 34.0% to HK$2.54 as compared to HK$1.90 in 2003.

Financial Position

As at 31st December, 2004, the Group was in a net cash position of HK$2,093 million as compared to HK$740 million in 2003. The Group maintained its high liquidity to meet the cost of the Milwaukee, AEG and DreBo acquisition and the need for additional working capital required after the acquisition. Free cash flow during the year increased from HK$1.26 billion in 2003 to HK$1.70 billion, an increase of 35.4%.

Net interest expense amounted to HK$86 million as compared to HK$79 million in 2003. The increase of just 9.0% was moderate given the expanded scale of the Group's operations. The Group will maintain efficient working capital management and capitalize on the relatively low interest rates. Interest cover, expressed as a multiple of profit before interest and tax over total net interest expenses, was 13.2 times as compared to 10.4 times reported in 2003.

Issue of Zero Coupon Convertible Bonds

On 16th June, 2004 the Group announced the issue of 5-year Zero Coupon Convertible Bonds at par. The aggregate principal amount of the Bonds was US$140 million (approximately HK$1,092 million). The Bonds will be due in 2009 and convertible into Ordinary Shares of the Company. The initial conversion price is HK$16.56 per share, representing a premium of 38% over the closing price of the share on The Stock Exchange of Hong Kong Limited on 16th June, 2004. Assuming full conversion of the Bonds at the initial conversion price of HK$16.56 per share, the Bonds will be converted into approximately 65,922,584 shares, representing approximately 4.93% of the issued share capital of the Company as at the date of announcement and approximately 4.71% of the issued share capital of the Company as enlarged by the issue of the conversion shares. Unless previously redeemed, converted or purchased and cancelled, the company will redeem each Bond at 107.76% of its principal amount on the maturity date of 8th July, 2009. However, on or after 8th July, 2007 and prior to the maturity date, the holder of each Bond will have the option to require the Company to redeem all or some of the Bonds at 104.59% of their principal amount.

The Bonds issued during the year raised immediate funds and was used for general corporate and working capital purposes including the financing of acquisitions. When converted, the issue will enlarge the shareholder capital base, which in turn will facilitate the development and expansion of the Group.

The issue of the Bonds was successfully closed on 8th July, 2004. No conversions were exercised during the year under review.

Bank Borrowings, Notes Issue

The Group now has a well-balanced and carefully-structured loan portfolio to support its long-term growth strategy and is also able to secure additional financing at favorable terms. Taking advantage of the low interest rate environment, the Group tapped into the capital market with two transactions in 2005 through its wholly-owned entity in the United States. The Group placed US Dollars two hundred million fixed interest rate Notes in two tranches, of US$150 million for 10 years at 5.44% per annum, and US$50 million for 7 years at 5.17% per annum, with private investors in the United States. Another US Dollars two hundred million LIBOR-based floating rate transferable term loan was arranged through an elite group of financial institutions for a 3-year period extendable to 5 years. Both issues received overwhelming support and were successfully closed in March 2005. The proceeds were used to refinance existing bank borrowings.

Foreign Exchange Risk Management

The Group's major borrowings are in US Dollars and HK Dollars. Other than the fixed interest rate Notes in issue during the year, all borrowings are based on LIBOR or Hong Kong best lending rates. As the Group's revenues are mainly in US Dollars, and major borrowings and payments are in either US Dollars or HK Dollars, there is a natural hedge mechanism in place and currency risk exposure is relatively low. However, the Group has strengthened its treasury management functions and will continue to manage its currency and interest rate exposures.

Working Capital

The Group's working capital remained strong with net current assets as at 31st December, 2004, of over HK$3.82 billion, an increase of 92.6% as compared to HK$1.99 billion in 2003. Current ratio further improved to 1.49 from 1.35 in 2003 and quick ratio was at 1.13 (2003: 0.91).

Inventory level increased by only 11.9% to HK$2.79 billion, despite a revenue increase of over 23.7%. Raw material and Work in Progress turnover days improved to 17 days as compared to 18 days in 2003. Finished goods turnover days increased by 3 days from 39 days to 42 days as compared to last year. All finished goods were subsequently shipped and delivered in January 2005.

Given the Group's high liquidity, no additional financing of receivables was arranged to contain finance costs. Trade receivables turnover days, therefore, increased from 45 days to 53 days. The Group is comfortable with current inventory and receivables turnover days, but will continue to improve its efficiency in this regard. During the year, the Group did not experience any material bad debts that required writing off.

As operations continued to expand, the Group managed to leverage its volume and secure favorable payment terms from suppliers and expanded financing arrangements through banks to optimize the current low interest rate environment. The Group has therefore been able to extend its trade credits by an additional 7 days as compared to last year.

Capital Expenditure

Capital expenditure during the year under review amounted to HK$312 million and was in line with the Group's depreciation charges for the year of HK$317 million.

Capital Commitment and Contingent Liabilities

As at 31st December, 2004, the capital commitment not provided for in respect of land in Dongguan, Mainland China amounted to approximately HK$18 million. Total capital commitment in 2004 amounted to HK$154 million (2003: HK$89 million).

As at 31st December, 2004, there were no material contingent liabilities or off balance sheet obligations other than trade bills discounted during the ordinary course of business.

Charges

None of the Group's assets are charged or subject to any encumbrance.

Acquisitions

On 28th August, 2004, the Group entered into a Stock Purchase Agreement to purchase from Atlas Copco AB ("ATCO") all of ATCO's electric power tools and accessories business ("the Business") conducted under the brand names "Milwaukee" and "AEG" as well as "DreBo" accessories businesses, ("the Sold Companies").

The transaction was approved unanimously by all the shareholders present in person or by proxy at the Company's Extraordinary General Meeting held on 3rd January, 2005 and was successfully closed on the same date.

The purchase price for the Business, which was paid in cash at the closing of the transaction, was US$627 million (approximately HK$4,887 million), consisting of the pre-adjustment purchase price of US$713 million (approximately HK$5,560 million), reduced by an agreed pre-closing adjustment of US$86 million (approximately HK$672 million) in respect of a portion of the accrued and unfunded post-retirement liabilities of certain of the Sold Companies and adjustments with respect to related deferred asset accounts and to certain accruals. The purchase price was calculated on the basis of the Sold

Companies having no indebtedness or cash and their net tangible assets (excluding, among other things, cash and amounts in respect of pre-agreed adjustments) being US$285 million (approximately HK$2,223 million). The parties are in the process of finalizing the closing statements for the Business and if the net tangible assets of the Business as shown in such agreed closing statements are less than US$285 million (approximately HK$2,223 million), the purchase price will be reduced by the amount of the shortfall. If the net tangible assets of the Business as shown in such agreed closing statements are greater than US$285 million (approximately HK$2,223 million), the purchase price will be increased by the amount of such excess.

The acquisition of the Business will enable the Group to enhance its leadership position in the global power tool industry. Through the acquisition, the Group acquired the Milwaukee brand, a well-established and widely recognized US power tool brand focused on professionals, and will gain access to the AEG brand, a well-recognized European power tool brand also focused on professionals. In addition, the Directors believe that the Sold Companies' engineering and design capability can be leveraged across the Group's existing product portfolio.

Major Customers and Suppliers

For the year ended 31st December, 2004:

i. The Group's largest customer and five largest customers accounted for approximately 39.8% and 62.8% respectively of the Group's total turnover.
ii. The Group's largest supplier and five largest suppliers accounted for approximately 4.2% and 18.2% respectively of the Group's total purchases (not including purchases of items which are of a capital nature).

According to the knowledge of the directors, none of the directors, their associates or any shareholders who owned more than 5% of TTI's share capital had any interest in the five largest customers or suppliers.

Human Resources

As at 31st December, 2004, the Group employed a total of 21,549 employees in Hong Kong and overseas (2003: 16,000 employees).

The Group continues to provide job-related training to all levels of staff to improve their skills and competencies as it believes that human capital is vital to its continuous growth and profitability.

The Group also offers competitive remuneration packages, discretionary share options and bonuses to all eligible staff based on individual and Group performances.

Investor Relations and Communications

The Group understands the importance of maintaining effective communication with our shareholders and the investment community. Regular meetings with analysts and institutional shareholders were conducted to promote investor relations and communications. The Company also maintains a website (www.ttigroup.com) which is updated on a timely basis to ensure all parties receive our latest corporate information.

Purchase, Sale or Redemption of Shares

There has been no purchase, sale or redemption of shares of the Company by the Company or any of its subsidiaries during the year.

Audit Committee

The Audit Committee is chaired by an independent non-executive director and all of the Committee members are independent non-executive directors. All Committee members possess appropriate professional qualifications, accounting or related financial management expertise as required under the Listing Rules. The Audit Committee has reviewed with management the accounting principles and practises adopted by the Group and discussed internal controls and financial reporting matters including a review of the audited final financial statements for the year ended 31st December, 2004.

Dividend

The Directors recommend a final dividend of HK12.50 cents per share. Subject to the approval of the shareholders at the Annual General Meeting to be held on 30th May, 2005. The final dividend will be paid to shareholders listed on the register of members of the Company on 17th June, 2005. It is expected that the final dividend will be paid on or about 29th July, 2005. This payment together with the interim dividend of HK4.50 cents per share paid on 30th September, 2004 makes a total payment of HK17.00 cents per share for 2004, an increase of 36.0% over that declared in 2003.

Closure of Register of Members

The Register of Members of the Company will be closed from Monday, 13th June, 2005 to Friday, 17th June, 2005, both days inclusive. In order to qualify for the final dividend to be approved at the Annual General Meeting, all transfers accompanied by the relevant share certificates must be lodged with the Company's Share Registrars, Secretaries Limited, at G/F, Bank of East Asia Harbour View Centre, 56 Gloucester Road, Wanchai, Hong Kong not later than 4:00p.m. on Friday, 10th June, 2005.

Dividend warrants will be despatched on or around 29th July, 2005 subject to shareholders' approval of payment of the final dividend having been obtained at the Annual General Meeting.